Service Area Redefinition
A Sensible Approach to Promoting the Twin Goals of
Advancing Universal Service and Facilitating Competition in Rural Areas

In Section 214(e)(5) of the 1996 Act, Congress permitted a "service area" to be defined as something other than a rural telephone company's study area so as to enable a competitor to be designated as an eligible telecommunications carrier ("ETC"). The process, known as service area redefinition, is critical for the advancement of universal service and the introduction of competition in all telecommunications markets. In competitive ETC ("CETC") designation proceedings across the country, service area redefinition has proven to be one of the more difficult issues for regulators to understand and implement.

As the Federal-State Joint Board on Universal Service ("Joint Board") considers this issue in the context of its ongoing universal service review, it is important to note that the Commission has before it several petitions from states to redefine rural incumbent local exchange carrier ("ILEC") service areas so as to permit CETC entry, some of which have been pending for over a year.[1] We will attempt to outline the problem and propose solutions that advance universal service, facilitate competitive entry, and ensure that no carrier is unfairly disadvantaged.

I. Background

Section 214(e)(5) of the Act provides that a CETC service area is defined as the rural ILEC's study area unless and until the state commission and the FCC, taking into consideration any recommendations from the Joint Board, redefine the rural ILEC's service area to be something other than its study area. Service area redefinition is necessary to advance universal service and permit competitive entry because no other class of telecommunications carrier is licensed along ILEC boundaries.[2]

Shortly after the 1996 Act, the Joint Board discussed factors to be considered when redefining ILEC service areas:

1. Whether the proposed service area redefinition raises concerns that the CETC is cream skimming;

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[1] *See, e.g.,* Petition by the Colorado Public Utilities Commission, Pursuant to 47 C.F.R. § 54.207(c), for Commission Agreement in Redefining the Service Area of Wiggins Telephone Association, a Rural Telephone Company, CC Docket No. 96-45 (filed May 30, 2003); Petition by the Public Utilities Commission of the State of Colorado to Redefine the Service Area of Delta County Tele-Comm, Inc., Pursuant to 47 CFR § 207(c), CC Docket No. 96-45 (filed Sept. 13, 2002); Petition of RCC Minnesota, Inc., for Redefinition of Rural Telephone Company Service Areas, CC Docket No. 96-45 (filed June 24, 2003); Petition of the Minnesota Public Utilities Commission for Agreement With Changes in Definition of Service Areas for Exchanges Served by CenturyTel et al., CC Docket No. 96-45 (filed July 8, 2003).

[2] For example, carriers in the Cellular Radiotelephone Service are licensed along MSA/RSA boundaries and, under the FCC's "unserved area" process, often have individual cell sites licensed in a rural area that are not contiguous with any commonly defined boundaries. PCS carriers are licensed along MTA/BTA boundaries. ESMR operators are licensed on a site-by-site-basis.

2. Whether the proposed service area redefinition will place an undue administrative burden on the ILEC; and

3. Whether the ILEC's status as a rural telephone company will be affected.[3]

In 1998, the Joint Board convened a Rural Task Force ("RTF") to study improvements in the universal service system for rural carriers and potential new entrants. Among its tasks, the RTF took up the question of how to minimize the possibility of CETCs receiving uneconomic support, while encouraging competitive entry.

The mismatch of CETC and rural ILEC service area boundaries prevents CETCs from serving throughout an ILEC study area. It follows that when a CETC enters, it should not receive uneconomic levels of support if its licensed area is limited to low-cost, or high-cost portions of an ILEC study area.[4] One solution to the boundary mismatch was to permit rural ILECs reallocate, or "disaggregate", support away from low-cost portions of their study areas and into high-cost portions of their study areas.[5] When a rural ILEC properly disaggregates support, it provides potential CETCs with an appropriate incentive to extend facilities to high-cost portions of the ILEC study area.[6] It also eliminates potential harm to a rural ILEC when a CETC is licensed to serve less than the ILEC's entire study area.[7]

In its 2001 *RTF Order*,[8] the FCC provided rural ILECs with three options to disaggregate support. Path 1 provided a no-disaggregation alternative for those rural ILECs that believed the process to be unnecessary. Rural ILECs retained the option to subsequently request disaggregation under Path 2 upon competitive entry. Disaggregation under Path 2 involved obtaining state approval, however it offered unlimited flexibility in designing a plan. Path 3 represented a self-certification option, which provided the ability to avoid a proceeding, but limited flexibility. The Commission intended that Path 2 or Path 3 disaggregation plans would

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[3] *See Federal-State Joint Board on Universal Service, Recommended Decision,* 12 FCC Rcd 87, 180 (Jt. Bd. 1996) ("*Recommended Decision*") The FCC adopted the Joint Board's recommendation in *Report and Order*, 12 FCC Rcd 8776 (1997).

[4] *See* Disaggregation and Targeting of Universal Service Support: Rural Task Force White Paper (Sept. 2000), available at http://www.wutc.wa.gov/rtf (RTF White Paper #6") at p. 5.

[5] *See Federal-State Joint Board on Universal Service,* CC Docket No. 96-45, Rural Task Force Recommendation to the Federal-State Joint Board on Universal Service (rel. Sept. 29, 2000) ("*RTF Recommendation*") at pp. 33-36.

[6] One thing the RTF did *not* recommend was for the CETC to be required to propose an ETC service area that represents 100% of its licensed service area within the state.

[7] *See* RTF White Paper #6 at p. 6 ("[T]here is reasonable consensus that disaggregation of universal service support into smaller geographic areas furthers the goals of the 1996 Act by benefiting the highest cost rural customers and enabling competitive entry").

[8] *Federal-State Joint Board on Universal Service Fourteenth Report and Order, Twenty-Second Order on Reconsideration, and Further Notice of Proposed Rulemaking*, 16 FCC Rcd 11244 (2001) ("*RTF Order*").

limit or reduce a CETC's support in low-cost areas and increase its support in high-cost areas, to provide the appropriate incentive for CETCs to enter.

On or before May 15, 2002, nearly ninety percent of the roughly 1300 rural ILECs chose Path 1, that is, they chose not to disaggregate support. Thus, in many cases where a CETC has entered, or is poised to enter, support continues to be available to the CETC in a single per-line amount throughout the ILEC's study area. If a study area is relatively homogeneous, this is not significant. However, where a study area's characteristics vary and the CETC is not licensed throughout an ILEC's study area, the CETC is either receiving more high-cost support than is appropriate (if it is licensed in low-cost areas) or is receiving less support than is necessary (if licensed in high-cost areas).

The rules adopted in the *RTF Order* envisioned the need for corrective action where an ILEC's initial Path selection proved to be inadequate. While providing that disaggregation plans would be effective for five years from the May 15, 2002, effective date, the new rules also allow rural ILECs to request Path 2 disaggregation if necessary to correct any unanticipated cost imbalances.[9] States may also order disaggregation on their own motion. Service area redefinition is a key tool in ensuring that CETCs have appropriate incentives to enter high-cost areas and do not receive significant high-cost support in low-cost areas.

II. Service Area Redefinition in Practice

On several occasions since the adoption of the FCC's service area redefinition rules, the FCC has concurred with states that have redefined rural ILEC service areas to enable competitive ETCs to be designated throughout their licensed service area. For example, in 1999, the FCC concurred with a proposal by the Washington Utilities and Transportation Commission and roughly 20 rural ILECs both to disaggregate support and to redefine each of the ILECs' service areas along wire center boundaries.[10]

The FCC similarly granted its concurrence with proposals to redefine ILEC services areas in Arizona and New Mexico to enable a wireless competitor to roll out service to Native Americans,[11] and with the Minnesota Public Utilities Commission's proposal to redefine the service area of Frontier Communications, Inc. Last year, the FCC concurred with the Colorado

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[9] *See* 47 C.F.R. §§ 54.315(b)(4); 54.315(c)(5); 54.315(d)(5).

[10] *See Petition for Agreement with Designation of Rural Company Eligible Telecommunications Carrier Service Areas and for Approval of the Use of Disaggregation of Study Areas for the Purpose of Distributing Portable Federal Universal Service Support, Memorandum Opinion and Order,* 15 FCC Rcd 9924, 9927-28 (1999).

[11] *See Smith Bagley, Inc. Petitions for Agreement to Redefine the Service Areas of Navajo Communications Company, Citizens Communications Company of the White Mountains, and CenturyTel of the Southwest, Inc. on Tribal Lands within the State of Arizona*, DA 01-409 (WCB rel. Feb. 15, 2001); *Smith Bagley, Inc. Petitions to Redefine the Service Area of Table Top Telephone Company on Tribal Lands within the State of Arizona*, DA 01-814 (WCB rel. April 2, 2001); *Smith Bagley, Inc. Petitions to Redefine the Service Area of CenturyTel of the Southwest, Inc. in the State of New Mexico*, DA 02-602 (WCB rel. March 13, 2002).

Public Utilities Commission's proposal to redefine the study area of CenturyTel of Eagle, Inc.[12] Other states, including Maine, Minnesota, West Virginia and Wisconsin, have similarly concluded that service area redefinition is appropriate to protect rural ILECs from uneconomic competition while permitting CETCs to enter.

To date, most ILECs that have gone through the service area redefinition process have had their single service area reclassified into multiple service areas, along wire center boundaries. In some cases, exchange boundaries have been used. Wire center or exchange boundaries are used primarily because they are familiar to the ILEC and are small enough to permit competitors in most instances to enter discrete territories. In addition, wire center or exchange area maps are generally available to permit regulators, incumbents, newly designated ETCs and subsequent entrants to easily understand the new service areas.[13]

III. Reducing the Possibility for Payment of Uneconomic Support.

Two important public policy objectives must be pursued in the service area redefinition process. First, ensure that the incumbent is treated fairly by preventing competitors from having an opportunity to cream skim or receive uneconomic support. Second, enable competitors to enter throughout their licensed territories so that they do not have unnecessary barriers to entry or a patchwork quilt of an ETC service area that works to the detriment of consumers.

In analyzing how to minimize cream skimming and uneconomic support, it is important to note that cream skimming is an intentional choice by a competitor to only serve low-cost areas. In ETC designation cases across the country, it has never been shown, and rarely even alleged, that a competitor is "picking and choosing" to enter only low cost areas of an ILEC in an attempt to improperly garner high-cost support.[14] This is because substantially all CETCs have to date proposed to serve throughout their licensed territory.

The potential for ***cream skimming*** can be eliminated by simply requiring CETCs to specify an ETC service area that comprises 100% of the CETC's licensed service area within the state. This step will remove any opportunity for a CETC to pick and choose its points of entry.

The problem of a CETC potentially receiving ***uneconomic support*** can be solved by making clear to states that ILEC requests to disaggregate support in response to competitive entry must be honored, absent extraordinary circumstances. If support is properly disaggregated,

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[12] *See, The Colorado Public Utilities Commission Petitions to Redefine the Service Area of CenturyTel of Eagle, Inc. in the State of Colorado*, DA 02-2087 (released August 26, 2002).

[13] Occasionally, disagreements over wire center or exchange boundaries have presented problems for states because competitors often do not have access to updated or accurate ILEC maps, which are not always on file with state commissions. Many maps have not been produced in a format that enables electronic duplication or the ability to overlay boundaries on a political map to properly orient a reader unfamiliar with ILEC telephone plant.

[13] Even if a CETC desired to cream skim (when an ILEC does not disaggregate support), a CETC does not have the information necessary to do so. Without detailed network cost information that is proprietary, unpublished, and available only to ILECs, it is impossible for a competitor to identify specific territory within an ILEC service area as being low-cost or high-cost.

CETCs will have an appropriate incentive to use available high-cost support to extend facilities to those areas that are most in need of improved facilities and will be precluded from receiving uneconomically high levels of support in low-cost areas.

IV. Solving the Problem of Partial Wire Centers.

Because CETC and ILEC boundaries are not congruent, there are often areas within an ILEC study area that cannot be reached by the CETC's facilities. Even when rural ILEC service areas are redefined to the wire center level, sometimes a CETC's licensed service area covers only part of one or more wire centers. Some have expressed concern that if a CETC serves only part of a wire center, there exists the possibility of a CETC receiving uneconomic support.

This concern can be resolved by appropriate disaggregation of support. If costs vary within a single wire center, the FCC has provided rural ILECs with the tools needed to alleviate the possibility of a competitor receiving uneconomic support. ILECs are permitted to specify up to two sub-zones under Path 3 and an unlimited number of sub-zones under Path 2. In rural wire centers where costs vary widely, if disaggregation is done properly, it matters not where a competitor enters because subsidies will only be available in high-cost areas.

Some have stated that when a CETC proposes to serve only a portion of a wire center, people living in the unserved portion are denied the benefits of competitive entry. This is undisputed,[15] but the solution is not to deny the benefits that a CETC is prepared to deliver throughout its entire service area. The more effective solution is proper disaggregation, which will increase the likelihood that the remaining portion of an unserved area will achieve competition. If the unserved area is a low-cost area, then other carriers are likely to enter without support (and probably already have). If it is a high-cost area, then other carriers have an incentive to enter as a CETC to gain support.

Properly targeting support to high-cost areas promotes efficient competitive entry and protects the incumbent's most desirable areas. It ensures that competitors receive the appropriate information to decide whether to enter the local exchange market as an ETC. Accurate disaggregation ensures that healthy competition in low-cost areas, which is already flourishing, will not be subsidized. In high-cost areas, competitors willing to commit to provide quality services will be encouraged to enter.

Some have claimed that if an ILEC service area is disaggregated to the wire-center level, then a competitor should be required to serve throughout the wire center. This solution forms a barrier to entry for competitors and has no corresponding practical advantages for consumers. To date, no party has identified a legitimate harm that befalls an incumbent if an competitor serves only part of a wire center.

Oftentimes, a CETC's proposed ETC service area touches numerous rural ILEC service areas, but may completely cover only a few. If the CETC's eligible service area is limited to only

[15] If competitive neutrality is properly taken into account, it is equally undisputed that a wireline ILEC's inability to serve portions of a wireless carrier's entire licensed area similarly deprives customers of the ILEC's competitive service.

those ILEC service areas that are covered completely, the resulting patchwork quilt of service areas significantly harms consumers. For example:

- Carriers are required to advertise the availability of Lifeline and Link-up benefits. Advertisements on radio, television, or newspaper do not respect arbitrary boundaries. Customers who would otherwise be Lifeline eligible will be denied benefits solely because they live in "ineligible areas".

- Planning and targeting network infrastructure development using high-cost support will be much more difficult. For example, the area served by new cell-site construction can overlap ineligible portions of the service area.

- A CETC would be prohibited from using high-cost funds to provide service to a requesting customer living on the wrong side of an arbitrary line.

- Operational changes made as a condition of ETC designation would have to be implemented throughout a network even though funding would only be available in part of the system.

Minnesota, Maine, and Colorado have all rejected rural ILEC claims of harm in the course of full litigation. In no state disaggregation proceeding has an ILEC demonstrated legitimate harm when service area redefinition and disaggregation are properly accomplished. Each market participant is free to compete throughout its respective service area and consumers are the beneficiaries.

V. Disaggregation of Support Will Deliver Market-Driven Competitive Entry.

Discussion of disaggregation leads necessarily to the question of just how many competitors should be permitted to enter in high-cost areas. Some have advocated artificial thresholds.

From a public-policy perspective, it would appear counterproductive to limit entry by a lower-cost competitor. The better policy is to encourage the lower cost providers to deliver the supported services so that support levels to an area can be minimized.

If implemented fully, proper disaggregation of high-cost support will send appropriate signals to competitive entrants. In the areas where costs are extreme, there may not be sufficient customer density to support multiple CETCs. Therefore, even the first CETC that seeks to enter will be forced to carefully examine whether it can keep its commitment to serve all requesting customers upon reasonable request.[16]

Because of low population density or extreme terrain (or both), a second or third CETC will be unlikely to make a business case for CETC entry with a facilities-based system that calls

[16] Again, if the CETC is forced to either serve 100% of the ILEC's study area or 100% of its own licensed service area, then such choices cannot be made based upon "picking and choosing" among ILEC service areas.

for service throughout its proposed ETC service area. Thus, subsequent competitors are more likely to forgo ETC status, or enter as an ETC using a combination of facilities and resale of either the incumbent or the first CETC to reach customers requesting service. Since only the facilities-based carrier receives the per-line support, customers served via resale will not generate high-cost support to the ETC.

In sum, the current system provides a self-correcting and market-driven mechanism to ensure that only the appropriate number of CETCs enter with a facilities-based network. Appropriate disaggregation, combined with a requirement to extend service to all consumers upon reasonable request imposes a market discipline that ensures competitors will enter based on rational business judgements and not arbitrage opportunities. It will also provide consumers in rural areas with as many competitors as the market will bear.[17]

VI. Case Illustration – Highland Cellular

The example of Highland Cellular, Inc., in West Virginia is instructive. Highland has applied for ETC status throughout its licensed ETC service area. The affected ILEC, Frontier Communications, has three study areas in West Virginia. Within each of its three study areas, Frontier has disaggregated support by grouping its wire centers into cost zones. As a result, in the densely populated portions of Highland's proposed ETC service area, it will receive no high-cost support ($0.00). This is appropriate because those areas are served by at least five wireless carriers, each of which may be able to offer service quality levels that permit competitive entry into the local exchange market.

In the sparsely populated portions of its service area, Highland will receive varying amounts of high-cost support, in some cases as much as $38.24 per month. Not coincidentally, some of these areas are completely without wireless service, while others have but one wireless carrier that does not offer service quality sufficient to advance universal service goals or permit competitive entry into the local exchange market.

At last count, approximately 79% of Highland's 10,176 lines would receive zero support because they are in low-cost areas. Thus, Highland will receive roughly a small fraction of the support received by the ILECs in its proposed ETC service area ***and*** it will be taking on the same commitment to offer service throughout the service area.[18]

Table 1 illustrates the support Highland would receive if the ILEC did not disaggregate support. Note that Frankford and Rupert are in different study areas operated by Frontier-controlled companies. The remaining wire centers are all within the same Frontier study area:

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[17] Recent proposals to restrict competitive entry in areas where per-line support exceeds certain thresholds fundamentally contravene the 1996 Act, which opens all markets to competition. Artificial barriers to entry are not only unlawful, but here, they prevent consumers in high-cost areas from receiving competitive alternatives that might otherwise be available if a lower-cost carrier believed it feasible to enter a market.

[18] Of course, Frontier will continue to get implicit support that is not available to competitors.

Table 1

Wire Center Name	Number of Customers	Support Available	Total
Athens	686	$11.92	$8,177.12
Bluefield	**3,470**	**$11.92**	**$41,362.40**
Bluewell	640	$11.92	$7,628.80
Bramwell	113	$11.92	$1,346.96
Matoaka	239	$11.92	$2,848.88
Oakvale	198	$11.92	$2,360.16
Princeton	**4,521**	**$11.92**	**$53,890.32**
Frankford	282	$37.72	$10,637.04
Rupert	27	$16.80	$453.60

Total Without Disaggregation: $128,705.28

Table 2 illustrates the support Highland will actually receive, taking into account Frontier's disaggregation plan:

Table 2

Wire Center Name	Number of Customers	Support Available	Total
Athens	686	$38.24	$26,232.64
Bluefield	**3,470**	**$0.00**	**$0.00**
Bluewell	640	$20.44	$13,081.60
Bramwell	113	$20.44	$2,309.72
Matoaka	239	$38.24	$9,139.36
Oakvale	198	$38.24	$7,571.52
Princeton	**4,521**	**$0.00**	**$0.00**
Frankford	282	$34.04	$9,599.28
Rupert	27	$23.80	$642.60

Total With Disaggregation: $68,576.72

Highland receives no support in Bluefield and Princeton (low-cost areas) and its total level of support is just over half of what it would be if the ILEC had not disaggregated. If Highland wishes to gain support, it can only do so by constructing facilities in the high-cost zones, which is precisely where a competitor should be focused – on consumers who currently have the fewest telecommunications choices.

These tables also demonstrate why it is not necessary for a CETC to serve an entire ILEC study area. The wire centers listed represent 100% of where Highland is licensed to serve, but are only a subset of the ILEC's study areas. The remaining areas within the state, assuming they are

also disaggregated, provide identical incentives for other carriers to enter as CETCs. If those areas are low-cost, then competition is likely already there. If they are high-cost, then disaggregation by the ILEC has provided support levels that will hopefully encourage other CETCs to enter the local exchange market.

VII. Consumers are Harmed when Resale is Required in Areas Where a Carrier is Not Licensed to Serve.

Some have advocated that a CETC should be required to offer services via resale in those areas of an ILEC's service area where it is not licensed to serve. There are numerous reasons why such an approach does not serve consumers' interests.

Imposing a resale requirement for CETCs would ignore the 1996 Act's goal of promoting facilities-based competition.[19] It would also directly contradict the FCC's conclusion that a primary benefit of competitive entry in rural areas is "the deployment of new facilities and technologies" as well as the creation of an "incentive to the incumbent rural telephone companies to improve their existing network to remain competitive."[20]

Because the FCC's rules no longer require wireless carriers to resell their services, a CETC is by no means assured of the continued cooperation of other wireless carriers or the ability to resell facilities pursuant to reasonable rates, terms, and conditions. Some states, such as Colorado, require a CLEC certificate to resell ILEC service. Outside of its own licensed service area, a CETC would not be able to control other carriers' wireless networks or service quality, leaving the CETC unable to provision service, improve service, or make any necessary network adjustments to provide an appropriate level of service to requesting consumers. If a facilities-based wireless carrier in a resale area is not an ETC, then it has no commitment to improve facilities in that area, further hamstringing the reselling ETC. The CETC would not be able to ensure that it could meet any ETC commitments, such as E-911 or toll limitation.

In addition, no high-cost support would be generated via resale of a non-ETC's network which means that consumers will see no benefit via improved facilities. The CETC could waste substantial portions of its high-cost support attempting to offer a resold wireline service to customers, which is truly no choice at all. Some states require a carrier to be a CLEC before it can resell ILEC service.

In sum, if consumer benefit is paramount, any requirement to provide resold services can only be properly applied within the CETC's licensed service area, where it has an incentive and ability to construct facilities. If a customer is not satisfied with resold service, the carrier would have the option (or perhaps be required) to construct facilities to provide appropriate service quality. Requiring resale outside of a carrier's licensed area provides no consumer benefit.

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[19] *See U.S. Telecom Ass'n v. FCC*, 290 F.3d 415, 424 (D.C. Cir. 2002).

[20] *See Western Wireless Corp.,* 16 FCC Rcd 48, 55 (2000). *See also* Remarks of Michael K. Powell, Chairman, Federal Communications Commission, at the Goldman Sachs Communicopia XI Conference, New York, NY (Oct. 2, 2002) ("Only through facilities-based competition can an entity bypass the incumbent completely and force the incumbent to innovate to offset lost wholesale revenues.")

VIII. Conclusion

The RTF, Joint Board and FCC have carefully developed service area redefinition policies that advance universal service and promote competition so that rural consumers may access to same kinds of choices as those that are available to people living in urban areas, in furtherance of Section 254 of the Act. Many states, including Colorado, Minnesota, West Virginia, New Mexico, Washington, Maine, and Arizona have implemented these policies to the benefit of consumers. RCA urges regulators to build on these policies to ensure that CETCs have a fair opportunity to enter all markets expeditiously to advance universal service.

The Rural Cellular Association